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REPORTS OF MALAYSIAN AND SINGAPORE CASES DETERMINED IN THE HIGH COURTS, THE FEDERAL COURT OF MALAYSIA, THE COURT OF APPEAL AND THE COURT OF CRIMINAL APPEAL OF SINGAPORE, AND THE PRIVY COUNCIL.

PRIVY COUNCIL REPORTS

AMERICAN LEAF BLENDING CO. SDN. BHD. v. DIRECTOR-GENERAL OF INLAND REVENUE

[P.C. (Lord Diplock, Viscount Dilhorne, Lord Edmund-Davies, Lord Russell of Killowen and Sir Robin Cooke)
June 6 and July 18, 1978]

[Privy Council Civil Appeal No. 12 of 1976]

Revenue Law — Income Tax — Company carrying on tobacco business — Company renting out premises — Liability to tax for rents — Whether company entitled to have losses from tobacco business set off against rental income — Whether rents income from a business — Income Tax Act, 1967, ss. 4, 24, 27 and 43.

This was an appeal from the decision of the Federal Court ([1975] 2 M.L.J. 26). The appellant company was incorporated with the object *inter alia* of carrying on a tobacco business. For this purpose it purchased land and built a factory. Subsequently the company found that it was not profitable to carry on the tobacco business and it ceased to do so. The land and buildings were let out to other companies. The company was assessed to income tax on the rental income and it sought to have the unabsorbed losses on the tobacco business and the unabsorbed capital allowances set off against the rental income. The claim was disallowed by the Director-General of Inland Revenue. On appeal it was allowed by the Special Commissioners who at the request of the Director-General stated a case for the opinion of the High Court. Hashim Yeop A. Sani J. ([1974] 2 M.L.J. 76) upheld the Company's claims to be entitled to deduction of the unabsorbed adjusted losses but he held that the unabsorbed capital allowances could not be taken into account in computing the income from the rents of the Company. On appeal the Federal Court allowed the appeal of the Director General and held that the unabsorbed losses from the tobacco business could not be deducted from the rental incomes; they agreed with the learned judge that the unabsorbed capital allowances could not be taken into account even if the renting of the premises could be assumed to be a business. The Company appealed. The question which arose on the appeal was: "Were the rents received by the Company for the letting of its premises or parts thereof to other persons for use of storage, income from a 'source consisting of a business' for the purposes of section 43(1)(a) and (2) of the Income Tax Act, 1967?"

Held: (1) rents despite the fact that they were referred to in paragraph (d) of section 4 of the Income Tax Act, 1967 might nevertheless constitute income from a source consisting of a business if they were receivable in the course of carrying on a business of putting the taxpayer's property to profitable use by letting it out for rent;

(2) upon the evidence in this case there was only one conclusion of fact that any reasonable Commissioners could reach viz. that there was nothing in the evidence capable of rebutting the *prima facie* inference that in the relevant periods of assessment the company was carrying on the business of letting out its premises for rent. On the contrary the evidence served only to reinforce the *prima facie* inference.

Cases referred to:-

(1) *Fry* v. *Salisbury House Estate Ltd.* [1930] A.C. 432.

(2) *Commissioners of Income Tax* v. *Hanover Agencies Ltd.* [1967] 1 A.C. 681.

(3) *Inland Revenue Commissioners* v. *Westleigh Estates Co.* [1924] 1 K.B. 390, 409.

PRIVY COUNCIL APPEAL FROM MALAYSIA.

D.K. Rattee Q.C. for the appellants.

P. Medd Q.C. and *C. Barthorst Q.C.* for the respondent.

Cur. Adv. Vult.

Lord Diplock (delivering the judgment of the Board): The appellant taxpayer ("the Company") was incorporated in 1960. The principal object for which it was established was to cut and blend tobacco and to manufacture cigarettes; but, as is usual, its Memorandum of Association incorporated a wide variety of objects including granting licences over and generally dealing with the land rights and other property of the Company.

The Company purchased land in Petaling Jaya whereon it erected a building, which contained a factory in which cigarette-making machinery was installed and a bonded warehouse for storing tobacco and cigarettes. The Company started to manufacture cigarettes there in February 1961; but this proved so unprofitable that the manufacturing business was abandoned in November of the same year and thereafter until 1964 its activities were confined to trading in tobacco. This likewise proved unprofitable and was in turn abandoned in 1964, by which time the Company had accumulated adjusted losses for income tax purposes amounting to $399,303.

With the abandonment of trading in tobacco the Company no longer needed to make use itself of the storage space provided by the bonded warehouse. So in April 1964, it licensed Caxton Press (1957) Ltd. to occupy and use the warehouse for storing paper on what was in effect a monthly tenancy. It is convenient to refer to this and subsequent licences as "lettings" and payments made thereunder as "rents" since they fall within the definition of "rent" in the Income Tax Act, 1967. It does not appear when this first letting ended; but on January 18, 1965 there was a fresh letting of the warehouse to a new licensee Zuellig Feedmills (Malaya) Ltd. for storing maize. This was a letting until May 31, 1965, terminable then or at any time thereafter on one month's notice. This second letting of the warehouse was followed by a third on

October 1, 1966 to Dunlop Malayan Industries Ltd. to store its own goods. This was a three months' letting; it does not appear whether this licensee in fact held over after the expiry of the three months.

In the course of 1967 the cigarette-making machinery which had remained *in situ* in the factory was sold and removed, thus making the factory as well as the warehouse available for letting for storage purposes. On January 30, 1967, the Company let the factory area to Tien Wah Press (Malaya) Ltd. for three months terminable on April 30, 1967 or at any time thereafter on one month's notice.

Finally on October 1, 1968 the factory and warehouse were let to Gammon South East Asia Berhad for storage purposes for twelve months terminable on September 30, 1969 or at the end of any subsequent month on six months' notice.

In the years of assessment 1968 and 1970 the Company was assessed to income tax under section 4(d) of the Income Tax Act, 1967, in respect of rents from these lettings. There is no dispute about the figures which amount to $7,040 in 1968 and $33,234 in 1970. The Company, however, claim to be entitled under section 43(1)(a) and (2) to set off against these, and any subsequent assessments, the accumulated adjusted loss of $399,303 until it is exhausted.

The claim was disallowed by the Director-General of Inland Revenue. On appeal it was allowed by the Special Commissioners who, at the request of the Director-General, stated a Case for the opinion of the High Court. The High Court (Hashim Yeop A. Sani J.) upheld the Company's claim to be entitled to deduction of the unabsorbed adjusted loss; but Hashim Yeop A. Sani J.'s decision on this matter was reversed by the Federal Court (Gill C.J., Ong F.J., Suleiman F.J.). It is from the judgment of the Federal Court that this appeal is brought.

Before the Special Commissioners and in both courts below the Company claimed that it was also entitled to set off against its income from the letting of its property the balance of unabsorbed capital allowances in respect of its tobacco manufacturing business. This claim was rejected by the High Court and the Federal Court. It has been abandoned before their Lordships, who are accordingly concerned only with the appellant's claim under section 43, to have deducted from the assessments on the Company to income tax for 1968 and 1970 the unexhausted balance of adjusted losses incurred in carrying on its tobacco business between 1961 and 1964.

Section 43, under which adjusted losses from a business of the taxpayer for previous years of assessment (as ascertained under section 40) are to be deducted from the aggregate of the taxpayer's statutory income for any year for the purpose of ascertaining his chargeable income for that year, draws a distinction between income from "a source consisting of a business" and income from any other source. It is only against income from a source consisting of a business that adjusted losses from a business for previous years of assessment can be set off. The taxpayer's business from which the previous loss was incurred, however, need not be the same business as that from which his statutory income for the year of assessment is derived. So the only question in this appeal is: Were the rents received by the Company for letting its premises or parts thereof to other persons for use for storage, income from "a source consisting of a business" for the purposes of section 43(1)(a) and (2) of the Act?

In support of the contention that they were not, two arguments have been advanced on behalf of the Inland Revenue. The first is general: that as a matter of construction of the Income Tax Act, 1967, income derived from the receipt of rents of premises is incapable of constituting income from a source consisting of a business. The second is special to the instant case: that on the facts found by the Special Commissioners the Company in the years of assessment 1968 and 1970 was not carrying on a business of letting out its premises or, it would seem, any other business at all.

The first and general argument on the construction of the Act failed in both courts below. It can be dealt with shortly by their Lordships. It is based upon the charging sections, section 4, which reads as follows: —

"4. Subject to this Act, the income upon which tax is chargeable under this Act is income in respect of —

(a) gains or profits from a business, for whatever period of time carried on;

(b) gains or profits from an employment;

(c) dividends, interest or discounts;

(d) rents, royalties or premiums;

(e) pensions, annuities or other periodical payments not falling under any of the foregoing paragraphs;

(f) gains or profits not falling under any of the foregoing paragraphs."

The contention is that paragraphs (a) to (e) refer to five separate classes of income that are mutually exclusive, in the same way as the various Schedules of the United Kingdom Income Tax Act, 1918 were held to be mutually exclusive by the House of Lords in *Fry* v. *Salisbury House Estate Ltd.*[1] As was pointed out by the Judicial Committee in the Jamaican appeal *Commissioner of Income Tax* v. *Hanover Agencies Ltd.*[2] the *Salisbury House* case turned on the peculiar structure and provisions of the United Kingdom Act, and threw no light upon the construction of other taxing statutes such as those of Jamaica or Malaysia whose structure and provisions are quite different.

If the words in the various paragraphs of section 4 of the Malaysian Act are given their ordinary meaning — and their Lordships see no reason why they should not be — there is plainly room for overlapping between one paragraph and another. A company may carry on business as an investment or holding company deriving its gains or profits from dividends and interest from the securities it owns. The gains or profit from the business of a bank or moneylender are largely derived from interest received on money lent. A property company or an individual may be carrying on the business of letting premises for rents from which the gains or profits of that business are derived.

That there is potential overlapping between paragraph (a) and paragraphs (c) and (d) is, in their Lordships' view, put beyond doubt by the provisions of section 24. The general rule laid down in sections 27 and 28 is that income other than income from a business does not become chargeable until it has actually been received. By section 27(1) this is applied specifically to "rent". The purpose of section 24 is to provide as an exception to the general rule that on computing chargeable income from a business book debts arising in the period of assessment shall be brought into account although not actually received. Sub-sections (4) and (5) apply this exception to dividends and interest on securities held by investment companies and interest receivable in the course of carrying on a business of lending money; while subsection (1)(c) applies the same exception *inter alia* to debts arising "in respect of ... (c) the use or enjoyment of any property dealt with at any time in the course of carrying on a business."

So it is clear that "rents", despite the fact that they are referred to in paragraph (d) of section 4, may nevertheless constitute income from a source consisting of a business if they are receivable in the course of carrying on a business of putting the taxpayer's property to profitable use by letting it out for rent.

Where premises are let in the course of carrying on the business of putting them to profitable use, section 43(1) in their Lordships' view gives primacy to the classification of the rents receivable as income from a source consisting of a business, notwithstanding that they may also be classified under section 4(d) as "rents". What section 43(1) requires is that one should first determine whether the rents are income from a business. If they are, no further inquiry is necessary; adjusted losses from a business of the taxpayer for previous years of assessment are deductible in ascertaining the taxpayer's aggregate income. Thus on the question of construction of the Act their Lordships are in agreement with the High Court and the Federal Court.

On the question special to the instant case, viz. whether the Company in 1968 and 1970 was carrying on a business of letting out its premises for rents, the Special Commissioners were of opinion that it was. The question is one of fact, and in the High Court Hashim Yeop A. Sani J. treated this expression of opinion as a finding of fact by the Commissioners which he should not disturb. Closer analysis of the Stated Case, however, discloses that the opinion expressed by the Special Commissioners was not a finding of fact but a conclusion of law. They accepted the Company's submission that because the letting of its property was one of the objects set out in its Memorandum of Association this was in law conclusive that in making any letting of its premises it was carrying on a business.

So stated this is, in their Lordships' view, too broad a proposition. It derives apparent support from an observation of Pollock M.R. in *Inland Revenue Commissioners* v. *Westleigh Estates Co.*,[3] where he said:

"If [a company's] objects are business objects and are in fact carried out it. . . carries on business."

This, however, was said in the context of a company which was carrying out one of the principal objects stated in its Memorandum. Their Lordships would not endorse the view that every isolated act of a kind that is authorised by its Memorandum if done by a company necessarily constitutes the carrying on of a business.

On the other hand their Lordships do not think that the dicta to be found in some of the speeches in the *Salisbury House* case and in particular those of Lords Warrington of Clyffe and Macmillan upon which the Federal Court relied and which suggest that the letting of land does not constitute a "trade", have any relevance to the question whether the letting of land by the Company in the instant case amounted to the carrying on of a "business" within the meaning of the Malaysian Income Tax Act, 1967. "Business" is a wider concept than "trade"; and in the *Hanover Agencies* case the Board uttered a warning against seeking to apply these dicta outside the narrow context of British income tax law and in particular that of Schedule D.

In the case of a private individual it may well be that the mere receipt of rents from property that he owns raises no presumption that he is carrying on a business. In contrast, in their Lordships' view, in the case of a company incorporated for the purpose of making profits for its shareholders any gainful use to which it puts any of its assets *prima facie* amounts to the carrying on of a business. Where the gainful use to which a company's property is put is letting it out for rent, their Lordships do not find it easy to envisage circumstances that are likely to arise in practice which would displace the *prima facie* inference that in doing so it was carrying on a business.

The carrying on of "business", no doubt, usually calls for some activity on the part of whoever carries it on, though, depending on the nature of the business, the activity may be intermittent with long intervals of quiescence in between. In the instant case, however, there was evidence before the Special Commissioners of activity in and about the letting of its premises by the Company during each of the five years that had elapsed since it closed down its former tobacco business. There were three successive lettings of the warehouse negotiated with different tenants; there was the removal of the machinery from the factory area which made it available for use for storage and a separate letting of that area to a fresh tenant; and as recently as October 1968 there was the negotiation of a letting to a single tenant of both the factory area and the warehouse.

As has been mentioned, the question whether the Company were carrying on a business of letting out their premises for rent was one of fact for the Special Commissioners: but it is one to which they did not apply their minds because of their mistake of law as to the effect of the presence in the Company's Memorandum of power to let their premises or any part thereof. Nevertheless their Lordships do not find it necessary to require the case to be remitted to the Special Commissioners for further consideration; for, in their Lordship's view, upon the evidence to which they have referred there is only one conclusion of fact

that any reasonable Commissioners could reach, viz. that there is nothing in the evidence capable of rebutting the *prima facie* inference that in the relevant periods of assessment the Company was carrying on a business of letting out its premises for rent. On the contrary the evidence serves only to reinforce that *prima facie* inference.

Their Lordships will advise His Majesty the Yang di-Pertuan Agong that the appeal be allowed, the order of the Federal Court set aside and the order of the High Court restored. They will further advise that the respondent pay the costs of this appeal but that there be no order as to the costs in the Federal Court or the High Court.

Appeal allowed.

Solicitors: *Freshfields; Stephenson Harwood.*

INTERNATIONAL INVESTMENT LTD. v. COMPTROLLER-GENERAL OF INLAND REVENUE

[P.C. (Lord Diplock, Viscount Dilhorne, Lord Fraser of Tullybelton, Lord Keith of Kinkel and Sir Robin Cooke) June 19, 20 and July 18, 1978]

[Privy Council Appeal No. 20 of 1976]

Revenue Law — Income Tax — Transfer of immovable property by company to another company in exchange for shares — Isolated transaction — Whether it constituted carrying on of a trade or business — Whether profits liable to income tax — Income Tax Ordinance, 1947, s. 10(1)(a).

This was an appeal from the decision of the Federal Court ([1975] 2 M.L.J. 208). The appellant company, one of whose objects was to traffic and otherwise deal in or turn into account immovable property, had acquired certain lands and had begun building operations on the lands. Subsequently it agreed to sell the lands and the uncompleted building on it to another company in exchange for shares in the company. These shares were subsequently transferred by the company. The company was assessed to tax on the profits obtained by it. On appeal the Special Commissioners upheld the assessment and a further appeal to the High Court by way of case stated was dismissed ([1973] 2 M.L.J. 10). An appeal from the judgment of the High Court was dismissed by the Federal Court and the appellant company appealed. It was argued on behalf of the appellant that the profit was not and could not be taxable as income under section 10(1)(a) of the Income Tax Ordinance, 1947, because the transaction from which it was received was an isolated transaction which did not constitute the carrying on of a trade or business. It might have been an adventure in the nature of trade but it could not have been trading because trading necessarily involved some repetition or continuity of operation and that element was lacking in the case. It was also argued that in any event the facts showed that when the appellant company acquired and developed the property, it was not trafficking or dealing in land but was investing in land, and any profit on the realisation of its investment was not of an income nature and was not assessable to income tax.

Held, dismissing the appeal: (1) a company whose business is or includes trading *prima facie* begins to trade as soon as it embarks upon the first transaction of a trading nature. The transaction in this case could therefore constitute trading even if it was isolated;

(2) there was evidence in this case on which the Special Commissioners could conclude that the appellant company was carrying on a trade in immovable property and there was no justification for reversing the determination of the Special Commissioners as it had not been shown that they had misdirected themselves in law or proceeded without sufficient evidence in law to justify their conclusion.

Cases referred to:-

(1) *D.E.F. v. Comptroller of Income Tax* [1961] M.L.J. 55.

(2) *E. v. Comptroller-General of Inland Revenue* [1970] 2 M.L.J. 117.

(3) *American Leaf Blending Co. Sdn. Bhd. v. Director-General of Inland Revenue* [1978] 2 M.L.J.

(4) *Commissioner for Inland Revenue v. Leydenberg Platinum Ltd.* [1929] S.A.L.R. 137.

PRIVY COUNCIL APPEAL FROM MALAYSIA.

Barry Pinson Q.C. (*John Gardiner* and *T.F. Chong* with him) for the appellant.

P. Medd Q.C. (*N. Lyell* with him) for the respondent.

Cur. Adv. Vult.

Viscount Dilhorne (delivering the judgment of the Board): The issue raised in this appeal is whether the Special Commissioners of Income Tax in Malaysia were entitled on the facts before them to find, as they did, that a profit made by the appellant company on realisation of immovable property was chargeable to income tax under the Income Tax Ordinance, 1947. The appellant company appealed by way of Case Stated against the determination of the Special Commissioners, and their appeal was dismissed by the High Court of Malaya (H. S. Ong J.). An appeal from his judgment was dismissed by the Federal Court of Malaysia (Gill C.J. Malaya, Raja Azlan Shah F.J. and Wan Suleiman F.J.). The present appeal is against the judgment of the Federal Court.

The appellant company was incorporated in 1962 with the objects *inter alia* of trafficking and otherwise dealing in or turning to account lands buildings and immovable property of any description. Its Memorandum of Association also included a wide variety of other objects including developing land and investing in shares and securities. Its authorised share capital was originally $500,000 in shares of $100 each, increased in 1963 to $5 million. On December 31, 1962 its issued share capital was $300,000 fully paid. By December 31, 1963 this had been increased to $500,000, and application and allotment moneys of a further $500,000 had been received for shares which had not then been allotted. In 1962 and 1963 it purchased several pieces of land in Penang Road, Penang, which together formed a block, for a total price of $337,273.71. After paying compensation to occupiers of some old houses on part of the land, it demolished the existing houses and entered into contracts for erection of a six storey shopping arcade and hotel to be known as the International Building. In 1962 it entered into negotiations for letting the proposed hotel but the negotiations proved abortive. In 1963 it received rents of $7,044.00 from the arcade.

On October 16, 1963 at an Extraordinary General Meeting of the members of the appellant company the following Special Resolutions were passed:

"1. That the business and undertaking of the Company be reconstructed and after such reconstruction to expand its business of investments in and the holdings of securities.

2. That the Company do convey its property known as Lots Nos. 14(1), 14(2), 15(2), 16(1), 30, 31 and 32 T.S. 16 N.E.D. Penang, together with the building erected thereon to Island Hotels & Properties (Malaysia) Limited in consideration of the issue of 2,846,300 shares of $1 each in the said Island